No. 97-829

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

MCI TELECOMMUNICATIONS CORPORATION,
Petitioner,

v.

IOWA UTILITIES BOARD, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

PETITIONER'S REPLY BRIEF

THOMAS F. O'NEIL III
WILLIAM SINGLE, IV
MCI TELECOMMUNICATIONS CORPORATION
1133 19th Street, N.W.
Washington, D.C. 20036
(202) 736-6412

BRUCE J. ENNIS, JR.*
DONALD B. VERRILLI, JR.
MARK D. SCHNEIDER
ANTHONY C. EPSTEIN
JENNER & BLOCK
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000
Counsel for Petitioner
* Counsel of Record

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ARGUMENT

Although respondents cumulatively devote one hundred and fifty pages to opposing certiorari, they do not seriously contest that the petitions present questions of national importance that have not previously been decided by this Court. The case involves a profound jurisdictional dispute between federal and state regulators over the proper scope of their respective authority to implement the local competition provisions of the landmark Telecommunications Act of 1996, and an important substantive dispute about how new entrants such as MCI will be allowed to compete in local markets. Respondents' principal argument against plenary review of these issues is that the Eighth Circuit correctly resolved them. As the petitions for certiorari demonstrated, that is not so. In any event, this Court, and not a single court of appeals, should pronounce the last word on such matters of nationwide importance.

A. Respondents' Arguments Confirm That the Eighth Circuit's Decision to Invalidate Section 51.315(b) of the FCC's Rules Presents a Question of National Importance.

1. Most respondents do not deny that the invalidation of § 51.315(b) of the FCC's "combination" rules has severely set back prospects for local competition. Indeed the briefs in opposition are striking for what they do not say on this score. The State Commission Respondents and the National Association of Regulatory Commissioners ("the State Respondents"), for example, do not oppose certiorari on this issue. That is doubtless because these States recognize the importance of preventing the discriminatory conduct § 51.315(b) outlawed. Respondent GTE opposes certiorari on this question, but does not dispute that the Eighth Circuit's ruling is having enormous practical marketplace effects.

Only the Regional Bell Operating Company ("RBOC") respondents suggest that this issue is of "second level" importance (RBOC Brief in Opposition at 2 ("RBOC Br.")), but they have not sought to rebut the proof petitioners adduced about the decision's devastating effects. For example, the RBOCs do not deny that they are engaging in the discrimination permitted by the Eighth Circuit, or that their conduct has strangled local competition in its infancy. After all, the claim that the Eighth Circuit's invalidation of § 51.315(b) "effectively has killed off local competition" in much of the market was made not by petitioners but by independent telecommunications experts and investment analysts.[1] In other contexts (when it furthers their purposes), the RBOCs have frankly acknowledged the effect of the appeals court's ruling.[2] And the RBOCs say nothing about perhaps the most damning fact

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[1] *See* MCI's petition for certiorari at 13 n.16 ("MCI Pet.").

[2] *See* Reply Brief in Support of Application by BellSouth for Provision of In-Region, InterLATA Services in South Carolina, FCC CC Docket No. 97-208, at 20 (filed Nov. 14, 1997) ("AT&T gambled its local business on a misreading of the 1996 Act, and lost.").

of all: nearly two years after the Act's passage, incumbent monopolists still control 99% of the local market.

Indeed, as their very defense of the Eighth Circuit makes clear, whether incumbents can break apart existing combinations of network elements before providing them is an issue of central importance. GTE and the RBOCs argue at length that had the Eighth Circuit not invalidated § 51.315(b), new entrants would have been able to engage in purported "regulatory arbitrage . . . lead[ing] to massive pressure on basic service rates and enormous losses for incumbents." RBOC Br. at 22. They contend the Eighth Circuit's ruling was necessary to steer new entrants away from extensive use of unbundled network elements to enter local markets, forcing them instead to rely principally on resale, thereby protecting implicit universal service subsidies which they claim are built into the resale rates, but not into the rates for unbundled network elements. In view of the importance respondents attach to whether incumbents may break apart existing combinations of network elements before leasing them to new entrants, it is not plausible to argue that this is a "second order" issue unworthy of this Court's attention.

2. Nor have the incumbent local exchange carrier ("ILEC") respondents presented a persuasive argument that the Eighth Circuit decided the issue correctly. They make virtually no effort to defend the decision under *Chevron USA, Inc. v. National Resources Defense Council, Inc.*, 467 U.S. 837 (1984). That is no surprise; the decision is indefensible on those terms. Instead, respondents frankly argue policy, contending that the invalidation of § 51.315(b) was necessary to preserve implicit universal service subsidies. This argument is meritless: it holds local competition hostage to the completion of universal service reform, while Congress clearly intended local competition to come first.

First, the argument's premise is demonstrably false. Congress did *not* impose artificial costs on service through combinations of unbundled elements to impede this kind of competition until the completion of universal service

reform. Neither did the Eighth Circuit's equally invalid policy judgment rest on this ground. Instead, Congress expressly made all three forms of competitive entry (resale, facilities-based, and combinations of network elements) immediately available, and expressed no preference as between them. And it was Congress, not the FCC, that intended local competition through all three routes of entry to start "as quickly as possible," [3] while at the same time declining to make universal service reform a precondition for opening local markets to competition via any of these three entry strategies. Indeed, the incumbents' plea for protection of implicit universal service subsidies flies in the face of § 254 of the Act, which requires that "any [universal service] support mechanisms . . . should be explicit, rather than implicit as many support mechanisms are today." [4] In other words, the incumbents are arguing that the 1996 Act should be interpreted to protect the very implicit subsidies which Congress sought to extirpate. If the incumbent monopolists believe that universal service reform instead should precede widespread local competition, their complaint is with the Congress, and not with the FCC.

Second, the solution proposed by the monopolists bears no relation to the purported problem respondents have identified. The costs of pointless taking apart and recombining permitted by the Eighth Circuit's ruling are entirely unrelated to the costs of the alleged subsidies which the monopolists claim they wish to preserve.[5] Neither would

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[3] H.R. Rep. No. 104-204, 104th Cong., 1st Sess. at 89 (July 24, 1995).

[4] H.R. Conf. Rep. No. 104-458, 104th Cong., 2d Sess. at 131 (Jan. 31, 1996).

[5] As a result of the Eighth Circuit's ruling, incumbent monopolists will be able to impose these discriminatory costs whenever new entrants order any two or more elements in combination—not merely when new entrants seek to rely exclusively on unbundled elements to provide service. Thus, the incumbent can impose these discriminatory costs even if a new entrant has installed its own switch, and seeks only to lease two elements—the local loop to a

the discriminatory costs permitted by the Eighth Circuit ruling be phased out when universal service reform is completed.

Third, as a practical matter, there is no risk that the "cherry picking" respondents hypothesize would have any effect on the subsidies they assert justify their monopoly pricing before federal universal service reform is implemented on its scheduled date of January 1, 1999. Given the monopolists' overwhelming advantages of incumbency, competitors will not attract (or be able to serve) sufficient numbers of local customers in the twelve-month period before universal service reform should be completed. That is no doubt why Congress was not persuaded by these arguments, and mandated local competition in advance of universal service reform. Nor does the experience during the year that the combination regulation was in place before it was struck down by the Eighth Circuit support respondents' fear of "cherry picking:" new entrants have yet to make significant inroads on the monopolists' business and profits.

Fourth, and most importantly, it is clear that the Eighth Circuit was making fundamental decisions about national telecommunications policy, not following the plain meaning of § 251, when it invalidated § 51.315(b) of the FCC's rules. The Eighth Circuit accepted the incumbents' argument that it was important to add unnecessary costs to the provision of service through unbundled network elements in order to distinguish that service entry method from resale, even if that hobbled prospects for immediate local competition. But it is the very point of *Chevron* that such policy matters are left to the agency charged with implementing the law. That alone is sufficient reason for this Court to grant certiorari.

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subscriber's home and the interface box that attaches the loop to the inside wiring.

B. The Scope of the FCC's Authority to Administer the 1996 Act is a Matter of National Importance That Needs to be Settled Definitively by This Court.

1. Respondents have not advanced a persuasive defense of the Eighth Circuit's decision to strip the FCC of authority to implement the pricing requirements of § 251. To begin with, respondents' defense rests on an implausible characterization of the 1996 Act. As respondents would have it, the Eighth Circuit simply effectuated Congress' desire to avoid federal intrusion "on the States' traditional jurisdiction exclusively to oversee intrastate telephone service" by granting the States "considerable latitude to make individual policy choices" about pricing methodologies. RBOC Br. at 5, 20; *see also* GTE Brief in Opposition at 22 ("GTE Br."). Leaving aside the substantial constitutional difficulties that would be inherent in any such effort to deputize the States to set national policy (*see* MCI Pet. at 26), § 251 itself is a massive intrusion on "the States' traditional jurisdiction," supplanting state law with comprehensive and detailed federal requirements designed to foster competitive markets —including express federal requirements governing price. *E.g.*, 47 U.S.C. §§ 251(c)(2), (c)(3), (c)(4), 252 (d). Moreover, Congress indisputably gave the FCC authority to prescribe binding national rules governing many important requirements of § 251, including all the substantive unbundling requirements of § 251(c)(3), and many of the resale requirements of § 251(c)(4). FCC rules in those areas intrude on the States' traditional intrastate authority just as much as did the pricing rules invalidated by the Eighth Circuit. A plausible defense of the Eighth Circuit's ruling therefore cannot rest on broadbrush invocations of federalism; it must explain why Congress would have chosen to deny the FCC authority to implement one important subset of the federal requirements of § 251 while granting the FCC authority to implement other important requirements of the very same provision. Respondents have not even attempted such a defense.

To the contrary, in cases under § 252(e)(6) of the Act reviewing state commission arbitration decisions, the ILEC respondents have uniformly sought to *deny* state commissions the very latitude they now assert § 251 confers. As respondent SBC Communications Inc. explained in demanding *de novo* review of state commission interpretations of § 251, allowing state commissions interpretive latitude "would not advance uniform application of federal law from one State to the next," and could risk "50 different interpretations in 50 different states." [6] Respondent US West has likewise pressed for *de novo* review because of "the need for uniform construction of federal law," and because no state commission has "the nationwide perspective required to implement *federal* telecommunications policies." [7] Respondent GTE has likewise argued that state commission judgments are entitled to no deference, for the same reasons.[8]

The principal issue on which the ILEC respondents have pressed their plea for nationwide uniformity is the *pricing requirement of § 251*—the very matter they here contend the Eighth Circuit properly left to the States. Indeed, the ILEC respondents have uniformly challenged state commission decisions to apply forward-looking cost methodologies, on the ground that § 251 unambiguously requires state commissions to use embedded cost methodologies that prevailed during the monopoly era Congress sought to end.[9]

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[6] *Southwestern Bell Telephone Company v. AT&T Communications of the Southwest*, No. A-97-CA-132-SS, Motion for Summary Judgment of Southwestern Bell Telephone Company at 17 (W.D. Tex. filed Apr. 30, 1997) (*"SWB Motion"*).

[7] *US West Communications Inc. v. Thoms*, No. 4-97-CV-70082, US West's Opening Brief at 8-9 (N.D. Iowa filed May 12, 1997).

[8] *GTE Southwest, Inc. v. Wood*, No. M-97-078, Brief in Support of Motion for Summary Judgment at 16 & n.5 (S.D. Tex. filed Oct. 31, 1997) (*"GTE Motion"*).

[9] Respondent GTE, for example, contends that the Texas Commission's choice of a forward-looking TELRIC methodology "is a flat violation of the Act" because it does not guarantee GTE

The defense of state prerogatives advanced by the ILEC respondents in this Court as a reason to deny certiorari is thus unalloyed cynicism. They waive the banner of "decentralized decisionmaking" here, GTE Br. at 22, only because it suits their purpose of upholding the Eighth Circuit's decision to invalidate the procompetitive forward-looking cost methodology imposed by the FCC. In truth, however, the ILEC respondents agree with petitioners that § 251 should be read to impose a uniform federal pricing methodology. They disagree only over which branch of the federal government should impose it—the FCC in the exercise of its authority under § 251(d)(1) "to establish regulations to implement the requirements of [§ 251]," or the federal courts in the exercise of their authority under § 252(e)(6) to ensure that state arbitration decisions "meet the requirements of Section 251"—and over what that uniform pricing methodology should be.

The very fact that the ILEC respondents have advanced such arguments across the country in § 252(e)(6) litigation is a powerful reason why the petitions for certiorari should be granted. If, as petitioners contend here and as the ILECs have contended in federal district courts from Florida to California, the 1996 Act does not guarantee the States any significant discretion to make fundamental choices about pricing methodologies, then the essential premise of the Eighth Circuit's decision denying the FCC authority over pricing methodologies is invalid.

Furthermore, the existence of this nationwide ILEC campaign to impose a uniform federal embedded cost methodology refutes respondents' assertion that all methodological questions about price have been "settled" in the States. As a result of the Eighth Circuit's ruling, the pricing issue is anything but settled. Restoring the FCC's pricing rules would, however, go a long way toward set-

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recovery of its embedded costs. *GTE Motion* at 38-39. Respondent SBC Communications Inc. is likewise arguing in Texas that the state commission's "TELRIC methodology similar to the FCC's . . . ignores the plain language of § 252(d)(1)." *SWB Motion* at 22-23.

tling the issue. Federal courts would have a single standard to apply in resolving these dozens of pending cases. And, because (as respondents stress) most States have adopted methodologies modeled on the FCC's vacated regulations, reimposing the FCC's pricing rules would not have the disruptive effect claimed by respondents. To the contrary, reimposing the FCC's pricing rules would vindicate most States' choice of pricing methodologies, and end the turmoil generated by the ILECs' nationwide campaign to invalidate forward-looking pricing. Moreover, as to the significant minority of states that have *not* in substance adopted forward-looking pricing methodologies, review is warranted to assure compliance with the substantive requirements of the Act.

2. Although the State respondents' defense of the Eighth Circuit is not so cynical, neither have they offered anything approaching the compelling defense of the ruling below that would be necessary to justify a denial of certiorari in a case of such nationwide importance. Petitioners have not ignored the Eighth Circuit's "plain meaning" ruling. To the contrary, the petitions for certiorari have all argued that the Eighth Circuit fundamentally misread § 251(d)(1)— which authorizes the FCC "to establish regulations to implement the requirements of [§ 251]"—in concluding that this provision granted no substantive rulemaking authority.

In this regard, respondents have not offered any convincing reason in the statutory text for reading § 251(d)(1) as solely a time limit. According to the State respondents, if Congress had wanted to grant rulemaking authority, it would have instead drafted "plainer" language stating "that the FCC rules extended to all regulations necessary to implement section 251." State Respondents' Brief In Opposition at 10. Such a nuanced view of the requirements of "plain meaning" can hardly justify denying the FCC authority to implement the pricing requirements of § 251. And respondents fail even to acknowledge the most obvious difficulty with their position. If

§ 251(d)(1) does not confer rulemaking authority on the FCC to implement any requirements of § 251, what is the source of the FCC's authority to issue the regulations respondents concede the FCC has authority to issue? None of the specific provisions to which respondents point provides anything like the express grant of rulemaking authority respondents claim is needed. At most these provisions presuppose the existence of rulemaking authority, and condition the FCC's exercise of that authority. That is doubtless why no respondent quotes any of these provisions to support the proposition that they unambiguously grant rulemaking authority.

Second, respondents insist that because Congress gave state commissions the authority to set "rates," by negative implication it could not have intended to have the FCC establish a national methodology to be used in setting those rates. RBOC Br. at 13. But respondents acknowledge that the Act in fact is silent on this point, *id.*, and they studiously avoid the legal point made in the petitions: when an issue of statutory construction turns on the implications to be drawn from legislative silence, *Chevron* requires that the agency's interpretation be given deference. This the Eighth Circuit plainly did not do.

Thus, the Eighth Circuit's ruling is so seriously open to question that it cannot stand as the last word on the scope of the FCC's authority to implement this "unusually important legislative enactment." *Reno v. American Civil Liberties Union*, 117 S. Ct. 2329, 2337 (1997).

CONCLUSION

The petition should be granted.

Respectfully submitted,

THOMAS F. O'NEIL III
WILLIAM SINGLE, IV
MCI TELECOMMUNICATIONS CORPORATION
1133 19th Street, N.W.
Washington, D.C. 20036
(202) 736-6412

BRUCE J. ENNIS, JR.*
DONALD B. VERRILLI, JR.
MARK D. SCHNEIDER
ANTHONY C. EPSTEIN
JENNER & BLOCK
601 13th Street, N.W.
Washington, D.C. 20005
(202) 639-6000
Counsel for Petitioner

* Counsel of Record